FILED
NOV 23 1943
CHARLES ELMORE CROPLEY
CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

No. 500

HENRY BAKER,

Petitioner.

vs.

THE UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

DAVID GETZ,
HERBERT SPENCER LEMAN,
HERMAN H. KREKSTEIN,
Counsel for Petitioner.

INDEX.

Subject Index.

	Page
Petition for writ of certiorari	1
Opinions below	2
Jurisdiction	2
Question presented	2
Statutes involved	3
Statement of the case	3
Specification of errors to be urged	5
Rulings of the court below	5
Reasons why writ should be granted	5
Brief in support of petition	9
Conclusion	13

Table of Cases Cited.

Arkansas Corporation Commission v. *Thompson*, 313 U. S. 132	11
Banco Mexicano, etc., v. *Deutsche Bank*, 53 App. D. C. 266, 289 Fed. 924, affirmed in 263 U. S. 591	12
In re Gould Mfg. Co., 11 Fed. Supp. 644	12
Metropolitan Life Insurance Co. v. *United States*, 107 F. (2d) 311	12
Rand v. *United States*, 249 U. S. 503, 510	12
Tucker v. *Alexander*, 275 U. S. 228, 232	12
United States v. *Michel*, 282 U. S. 656, 660	12

Codes and Statutes.

Bankruptcy Act (52 Stat. 843), 11 U. S. C. A., Sec. 11 (a) (7)	3, 6, 11
Internal Revenue Code Sections 3674(b), 3675; 53 Stat. 449, 450; Title 26 U. S. C. A., Sections 3674(b), 3675	2, 3, 5, 6, 7
Judicial Code, Sec. 240(a) as amended, 43 Stat. 938, 28 U. S. C. A., Sec. 347	2, 3

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

No. 500

IN THE MATTER OF JAMES K. BOWEN,
BANKRUPT.

HENRY BAKER,

vs. *Petitioner,*

THE UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioner prays that a writ of certiorari issue to review the decree of the Circuit Court of Appeals for the Third Circuit, entered on September 2, 1943 (R. 138), reversing with directions, the decree of the District Court of the United States for the Eastern District of Pennsylvania, entered November 30, 1942 (R. 129a) 48 Fed. Supp. 67.

Opinions Below.

One opinion was delivered by the District Court. It was written by District Judge Harry E. Kalodner and filed November 30, 1942. It appears on page 115a of the Record and is reported in 48 F. Supp. 67. The opinion of the Circuit Court of Appeals (Circuit Judges Biggs, Goodrich and Woodbury, Judge Woodbury writing) was filed September 2, 1943, and appears at page 133 of the Record. (Case not yet officially reported.)

Jurisdiction.

Jurisdiction is invoked under Sec. 240(a) of the Judicial Code as amended by the Act of February 13, 1925, C. 229 (43 Stat. 938, 28 U. S. C. A. Sec. 347) and Sec. 24(c) of the Bankruptcy Act, as amended, 11 U. S. C. Ch. 4 Sec. 47. The judgment of the Circuit Court of Appeals was entered September 2, 1943.

This was an appeal from an order of the United States District Court for the Eastern District of Pennsylvania entered in a bankruptcy proceeding on November 30, 1942 (R. 129a) The order reversed two orders of the Referee in bankruptcy, striking off and vacating a discharge of real estate of the bankrupt from federal tax liens. The Circuit Court of Appeals for the Third Circuit reversed the District Court and remanded the case for further proceedings not inconsistent with its opinion (R. 138).

Question Presented.

Has a bankruptcy court the power to set aside or reverse a determination involving the valuation of property made by the Commissioner of Internal Revenue pursuant to the provisions of Sec. 3674(b) of the Internal Revenue Code upon an allegation that the determination was induced by constructive fraud?

Statutes Involved.

Bankruptcy Act (52 Stat. 843) 11 U. S. C. A. Sec. 11 (a) (7).

Internal Revenue Code Sections 3674(b), 3675; 53 Stat. 449, 450; Title 26 U. S. C. A. Sections 3674(b), 3675.

Judicial Code, Sec. 240(a) as amended, 43 Stat. 938, 28 U. S. C. A. Sec. 347.

Summary Statement.

The essential facts may be summarized as follows:

On August 12, 1933, federal income taxes in the amount of $15,297.68, plus accrued interest of $5,883.53 (a total of $21,181.21), were assessed against the bankrupt, James K. Bowen. In May, 1935, an assessment of $13,108.92 was made for distilled spirits taxes. Notices of the tax liens were duly filed pursuant to Sec. 3186 of the Revised Statutes, as amended by the Revenue Act of 1928, Sec. 613(a) (now Internal Revenue Code Sec. 3672).

Subsequently in September, 1935, Henry Baker, the petitioner herein, obtained a state court judgment against Bowen for $79,240.42. Since the notices of the tax liens were filed prior to Baker's judgment, the latter was inferior to them.

Bowen's principal assets consisted of certain ground and buildings at 809-811-813 Hamilton Street, Allentown, Pennsylvania. In December, 1938, Baker filed with the Commissioner of Internal Revenue an application for a certificate of discharge of the tax liens on this property, pursuant to the provisions of Sec. 3674(b) of the Internal Revenue Code (Appendix to brief filed with this petition.) On March 10, 1939, following an investigation, the Commissioner determined that the value of the interest of the United States in the real estate was less than $150.00 and authorized the Collector to issue the certificates of discharge upon payment

of $150.00. The said sum was paid and the discharges were issued and filed of record on April 14, 1939 (R. 40a).

Bowen filed a voluntary petition in bankruptcy seven months later on November 8, 1939. In August, 1940, the Hamilton Street property was sold at public sale by the trustee in bankruptcy for $457,500.00, less broker's commissions.

Thereafter, on the 27th day of January, 1941, the United States filed a petition with the Referee, alleging, *inter alia,* that the Commissioner in authorizing the discharge had been misled by Baker as to the value of the property and the amount of the indebtedness on various prior judgment liens. The petition requested the reinstatement of the liens theretofore discharged, as proper charges against the fund realized from the sale of the real estate.

An answer was filed by Baker after which, on hearing before the Referee over the objections of Baker, orders were entered allowing the Government's claims, striking off the discharges of the liens, reinstating the liens, and providing for payment of the Government's claims from the funds to be distributed in accordance with the priority created by the liens.

The District Court, on Baker's petition for review, reversed the orders of the Referee and ordered a distribution without regard to the tax liens. The decision of the District Court was based upon the ground that the Bankruptcy Court did not have jurisdiction to set aside the Commissioner's discharge of the liens and that the Referee erred in vacating or setting aside the discharge of the federal tax liens.

Thereupon the Government appealed to the Circuit Court of Appeals for the Third Circuit which reversed the lower court.

Specification of Errors to Be Urged.

The Circuit Court of Appeals erred:

1. In holding that the Bankruptcy Court has jurisdiction and power to set aside a certificate of discharge of real estate from federal tax liens, issued and recorded under express authorization of the Commissioner of Internal Revenue pursuant to the provisions of Sec. 3674(b) of the Internal Revenue Code.

2. In holding that Sec. 3675 of the Internal Revenue Code does not preclude the court from setting aside for "constructive fraud" a discharge of lien entered pursuant to Sec. 3674(b) of the Internal Revenue Code.

3. In reversing the order of the United States District Court.

Rulings of the Court Below.

The District Court held that the Bankruptcy Court is without jurisdiction in the matter, and that the Referee erred in vacating or setting aside the discharge of the federal tax liens.

A decree in conformity with the opinion of the District Court was thereupon entered.

The Circuit Court ruled that the decree of the District Court be reversed and the case be remanded for further proceedings not inconsistent with its opinion.

Reasons for Granting.

I. *The Circuit Court of Appeals has decided an important question of federal law which has not been, but should be, settled by this court.*

The District Court stated in its opinion, that despite an exhaustive investigation, it failed to find a single case

wherein was involved the vacation of a discharge of a lien, whether in bankruptcy or otherwise.

A conclusive decision on the jurisdiction of a Bankruptcy Court to set aside or reverse a determination involving the valuation of property made by the Commissioner of Internal Revenue, pursuant to Sec. 3674(b) of the Internal Revenue Code, would be of such importance as to warrant the granting of this petition, in view of the fact that it presents a novel question not heretofore settled by this court.

The Circuit Court of Appeals construed the provisions of the Bankruptcy Act (52 Stat. 843, 11 U. S. C. Sec. 11(a)(7)) which confer on the Courts of Bankruptcy the power to "Cause the estates of bankrupts to be collected, reduced to money and distributed and determine controversies in relation thereto," as conferring jurisdiction upon the court to hear and determine the question presented. Neither this court, nor any court of inferior jurisdiction, has heretofore had occasion to pass upon this moot question which is an important one of federal law.

II. *The Circuit Court of Appeals has decided a federal question in a way probably in conflict with applicable decisions of this court.*

In *Arkansas Corporation Commission, et al.* v. *Thompson, Trustee,* 313 U. S. 132, this court ruled substantially that there is nothing in the history of bankruptcy legislation to support the theory that Congress intended to set the federal courts up as super-assessment tribunals over state taxing agencies. Logically it should follow that the same lack of jurisdiction exists to review assessments or other phases of the assertion or discharge of liens for taxes by the Commissioner of Internal Revenue, especially in view

of the plain and unambiguous language of Sec. 3675 of the Internal Revenue Code which is as follows:

> "A certificate of release or of partial discharge issued under this subchapter shall be *conclusive* that the lien upon the property covered by the certificate is extinguished." (Emphasis supplied.)

For these reasons it is respectfully submitted that this petition should be granted.

DAVID GETZ,
HERBERT SPENCER LEMAN,
HERMAN H. KREKSTEIN,
Attorneys for Petitioner.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

No. 500

IN THE MATTER OF JAMES K. BOWEN, BANKRUPT.

HENRY BAKER,

Petitioner,

vs.

THE UNITED STATES OF AMERICA.

BRIEF FOR HENRY BAKER, PETITIONER.

The Facts.

The facts are stated in the petition, page 3. We emphasize that the decision of the District Court was based upon the ground that the Bankruptcy Court did not have jurisdiction to set aside the Commissioner's discharge of the tax liens and that the Referee erred in vacating or setting aside the discharges.

Argument.

I—*The Circuit Court of Appeals has decided an important question of federal law which has not been, but should be, settled by this court.*

The scope of the power and jurisdiction of a Bankruptcy Court, insofar as it applies to the single question here pre-

sented, constitutes an important question of federal law.

The Internal Revenue Code, Sec. 3670 (U. S. C. 1940 ed. Title 26) subjects all property and rights to property, whether real or personal belonging to any person who neglects or refuses to pay any tax, to a lien in favor of the United States.

The magnitude and value of property which thus becomes subject to the provisions of this Act is immediately apparent. It is of immeasurable importance therefore that the proper forum having jurisdiction of such a prolific source of vexatious disputes and litigation be properly and authoritatively defined by this court.

Sec. 3675 of this Act provides as follows:

> "A certificate of release or of partial discharge issued under this subchapter shall be held conclusive that the lien upon the property covered by the certificate is extinguished."

This section of the statute evidences a strong intention on the part of Congress that discharges of liens made under this section may not be revoked or set aside, especially in view of the fact that other Acts providing for compromise agreements between taxpayers and the Commissioner contain dissimilar provisions. Illustrative of the latter is the language of Sec. 1106 (b) of the Revenue Act of 1926, 44 Stat. 9, 113, which provides as follows:

> "* * * that such determination and assessment shall be final and conclusive (*except upon a showing of fraud or malfeasance or misrepresentation of fact materially affecting the determination or assessment thus made* * * *) and (2) no suit, action, or proceeding to annul, modify, or set aside such determination or assessment shall be entertained by any court of the United States." (Emphasis supplied.)

The fact that there was no such exception or reservation in Sec. 3675 is indicative of the intention of Congress.

It is submitted that the clarity and concise language of the Act may have precluded the possibility of a prior judicial determination of the jurisdiction of the Bankruptcy Court or of any other court upon this question. Whatever reason may be ascribed to the absence of such judicial expression, the District Court has said, and the Circuit Court of Appeals has not negatived the statement that despite an exhaustive search it has failed to find a single case where there was a vacation of a discharge of a lien, whether in bankruptcy or otherwise. Furthermore, in the instant case, the government frankly concedes that the action of the referee in vacating the discharge of the tax liens is without precedent (R. 126a).

The Circuit Court of Appeals cited no cases which support its reversal of the lower court, and, disregarding the plain language of Sec. 3675, found jurisdiction in the Bankruptcy Court under the general provisions of the Bankruptcy Act (52 Stat. 843, 11 U. S. C. Sec. 11 (a) (7)) which confers jurisdiction upon Courts of Bankruptcy to "Cause the estates of bankrupts to be collected, reduced to money, and distributed, and determine controversies in relation thereto."

II—*The Circuit Court of Appeals has decided a federal question in a way probably in conflict with applicable decisions of this court.*

The question as to whether a federal Bankruptcy Court has the power to revise or redetermine property valuations, for tax purposes, made by duly constituted taxing officials has been set at rest by the Supreme Court in the case of *Arkansas Corporation Commission* v. *Thompson,* 313 U. S. 132. In that case it was held that the valuation of property made by state taxing officials for taxation purposes could not be revised by a bankruptcy court; that there is nothing

in the history of bankruptcy legislation to support the theory that Congress intended to set the federal courts up as super-assessment tribunals over state taxing agencies.

In the case at bar the decision of the Circuit Court of Appeals would permit a determination of the value of property, made by the Commissioner of Internal Revenue for the purpose of fixing a consideration for the discharge of a federal tax lien, to be revised by a bankruptcy court.

The Commissioner in the instant case made a formal determination of the value of the interest of the United States in the real estate sought to be discharged from the tax liens. In so doing the Commissioner determined the value of the real estate. In order to find that the discharge was obtained by the alleged constructive fraud, the bankruptcy court was obliged to re-examine the value of the real estate and of the interest of the United States therein.

If the Arkansas case decided that a bankruptcy court has no jurisdiction to revise the valuation of property made by taxing officials for tax purposes, it would seem that the Circuit Court of Appeals decided the instant case in conflict with the decision of this court.

The instant decision of the Circuit Court of Appeals is likewise in conflict with the decisions handed down in:

In re Gould Mfg. Co., 11 F. Supp. 644;

Metropolitan Life Insurance Co. v. *United States,* 107 F. (2d) 311;

Banco Mexicano etc. v. *Deutsche Bank,* 53 App. D. C. 266, 289 F. 924, affirmed in 263 U. S. 591;

Rand v. *United States,* 249 U. S. 503, 510, 39 S. Ct. 359, 63 L. Ed. 731;

United States v. *Michel,* 282 U. S. 656, 660, 51 S. Ct. 284, 75 L. Ed. 598;

Tucker v. *Alexander,* 275 U. S. 228, 232, 48 S. Ct. 45, 72 L. Ed. 253.

Conclusion.

Your petitioner respectfully submits that the final determination by this court of the question of law involved in this case is of the utmost importance to the rights of taxpayers and others acquiring interests or equities in property of taxpayers subject to the provisions of the Act.

The decision of the Circuit Court of Appeals herein is the first judicial determination of the question presented. In addition to being a case of first impression on an important question of federal law, it is a decision which is probably in conflict with applicable decisions of this court.

Respectfully submitted,

DAVID GETZ,
HERBERT SPENCER LEMAN,
HERMAN H. KREKSTEIN,
Attorneys for Petitioner.

APPENDIX.

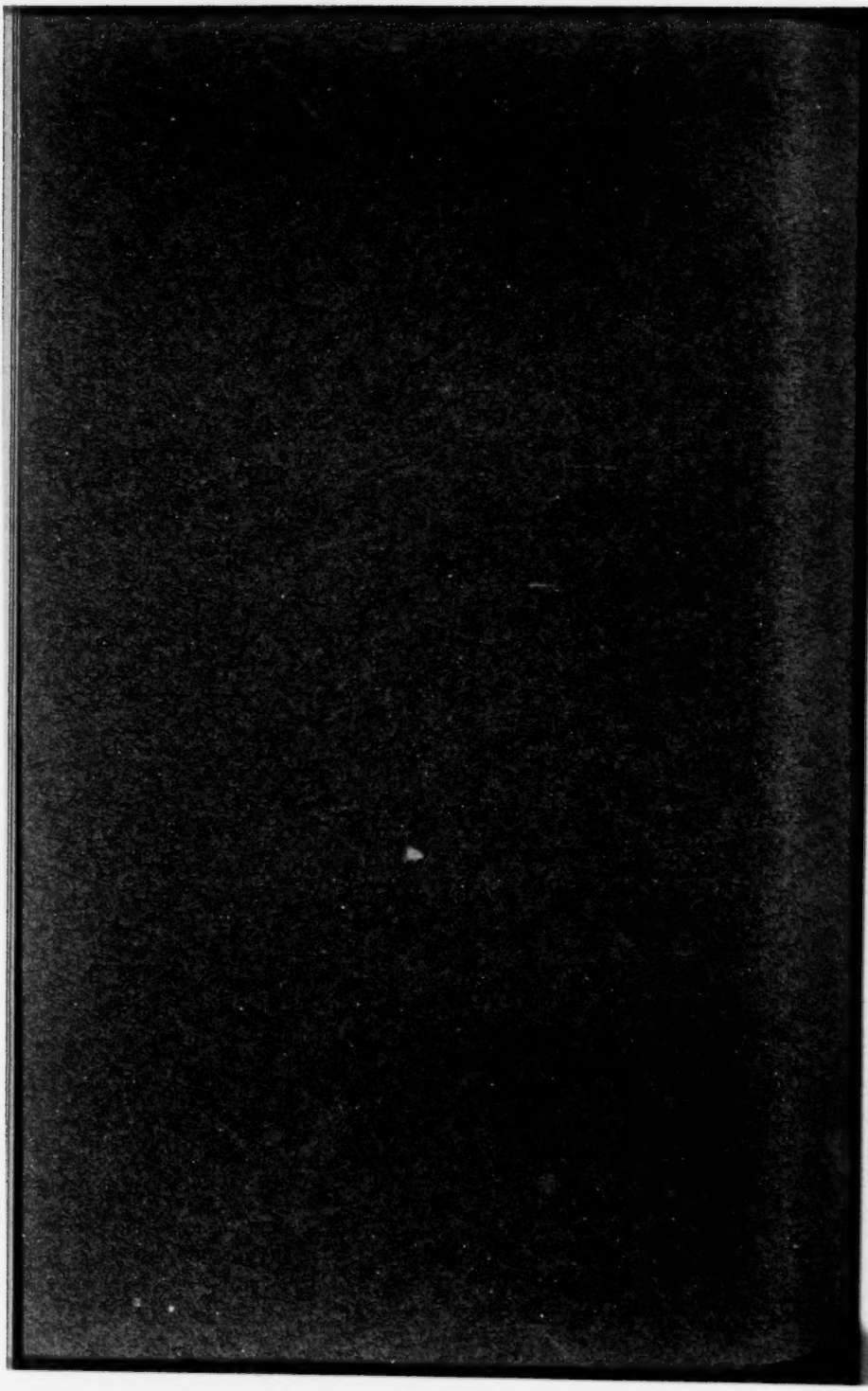
I.

Internal Revenue Code.

Sec. 3674. Partial discharge of property

(b) Part payment. Subject to such regulations as the Commissioner, with the approval of the Secretary, may prescribe, the collector charged with an assessment in respect of any tax may issue a certificate of discharge of any part of the property subject to the lien if there is paid over to the collector in part satisfaction of the liability in respect of such tax an amount determined by the Commissioner, which shall not be less than the value, as determined by him, of the interest of the United States in the part to be so discharged. In determining such value the Commissioner shall give consideration to the fair market value of the part to be so discharged and to such liens thereon as have priority to the lien of the United States. 53 Stat. 449; 28 U. S. C. A. 3674(b).

Sec. 3675. A certificate of release or of partial discharge issued under this subchapter shall be held conclusive that the lien upon the property covered by the certificate is extinguished. 53 Stat. 450; 26 U. S. C. A. 3675.



INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes involved	2
Statement	2
Argument	5
Conclusion	8
Appendix	9

CITATIONS

Cases:	
American Ins. Co. v. *Avon Park*, 311 U. S. 138	5
Arkansas Comm'n v. *Thompson*, 313 U. S. 132	7
Pepper v. *Litton*, 308 U. S. 295	5
Ray v. *Norseworthy*, 23 Wall. 128	7
Sampsell v. *Imperial Paper Corp.*, 313 U. S. 215	5, 6
Straton v. *New*, 283 U. S. 318	7
Taylor v. *Standard Gas Co.*, 306 U. S. 307	5
Statutes:	
Bankruptcy Act of July 1, 1898, c. 541, 30 Stat. 544, as amended by the Act of June 22, 1938, c. 575, 52 Stat. 840, Sec. 1:	
Sec. 2 (11 U. S. C. 1940 ed., Sec. 11)	7, 9
Sec. 38 (11 U. S. C. 1940 ed., Sec. 66)	10
Sec. 57 (11 U. S. C. 1940 ed., Sec. 93)	4
Sec. 64 (11 U. S. C. 1940 ed., Sec. 104)	7, 11
Sec. 67 (11 U. S. C. 1940 ed., Sec. 107)	11
Sec. 70 (11 U. S. C. 1940 ed., Sec. 110)	12
Internal Revenue Code:	
Sec. 3670 (26 U. S. C. 1940 ed., Sec. 3670)	12
Sec. 3671 (26 U. S. C. 1940 ed., Sec. 3671)	13
Sec. 3672, as amended (26 U. S. C. 1940 ed., Sec. 3672)	13
Sec. 3674 (26 U. S. C. 1940 ed., Sec. 3674)	13
Sec. 3675 (26 U. S. C. 1940 ed., Sec. 3675)	4, 14

564362—43

In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 500

HENRY BAKER, PETITIONER

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 114a–128a) is reported in 48 F. Supp. 67. The opinion of the Circuit Court of Appeals is not yet reported (R. 133–137).

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on September 2, 1943 (R. 138). The petition for a writ of certiorari was filed on November 23, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a bankruptcy court has power to set aside certificates of discharge of federal tax liens, issued by the Commissioner of Internal Revenue pursuant to Section 3674 (b), Internal Revenue Code, where the discharges of the tax liens were fraudulently obtained by a judgment creditor holding a junior lien upon the property.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 9–14.

STATEMENT

The relevant facts as found by the District Court may be summarized as follows:

On August 12, 1933, the Commissioner of Internal Revenue assessed federal income taxes against James K. Bowen in the amount of $21,181.21. In May 1935 an assessment was made against Bowen for federal distilled spirits taxes in the amount of $13,108.92. Notices of tax liens were duly filed within a few days of each assessment pursuant to Section 3186, Revised Statutes, as amended by the Revenue Act of 1928, Section 613 (a) (now Internal Revenue Code, Section 3672). (R. 115a–116a.) Subsequently in September 1935, Henry Baker, petitioner herein, obtained a judgment against Bowen in the Court of Common Pleas, Lehigh County, Pennsylvania, for $79,240.42. Since the judgment was obtained sub-

sequent to the filing of notices of liens it was, of course, inferior to the federal liens. (R. 116a.)

Bowen's principal asset was the ground and building located on Hamilton Street, Allentown, Pennsylvania. His other properties were mortgaged for more than their value. (R. 116a.) In December 1938, pursuant to Section 3674 (b), Internal Revenue Code, Baker filed an application for a discharge of the liens from the Hamilton Street property. On March 10, 1939, following an investigation the Commissioner authorized the Collector of Internal Revenue to issue certificates of discharge of the liens from the property upon payment of $150. The certificates were issued and filed of record on April 14, 1939. (R. 116a–117a.)

On November 8, 1939, Bowen filed a voluntary petition in bankruptcy. In August 1940 the bankruptcy trustee sold the Hamilton Street property at public sale for $457,500, less broker's commission. (R. 117a–118a.) The United States filed a petition with the referee alleging *inter alia* that the Commissioner had been misled by Baker as to the value of the property and the amounts of indebtedness on various prior judgment liens (R. 7a–15a). The petition prayed that the referee find that the federal liens were proper charges against the proceeds from the sale of the property and were prior to Baker's judgment (R. 15a). After an answer was filed by Baker there was a hearing before the referee, who allowed the Government's tax claims and set aside the discharge

of the federal tax liens, reinstated them and impressed them on the funds in the hands of the trustee, in accordance with a schedule of distribution which gave the Government priority over Baker as to the latter's judgment. (Referee's opinion, R. 68a–104a; Referee's orders, R. 64a–67a; Schedule of Distribution, R. 105a–108a.)

The referee found that the Commissioner was misled by false representations and omissions of material facts by Baker, which induced the Commissioner to authorize the issuance of certificates of discharge and which amounted to constructive fraud (R. 92a). Upon a petition for review filed by Baker, the District Court reversed the referee on the ground that the bankruptcy court had no jurisdiction to vacate or set aside the discharge of federal tax liens. The District Court did not pass on the merits.[1]

On appeal the Circuit Court of Appeals reversed and held (1) that Section 3675, Internal Revenue Code, which provides that "A certificate of release or of partial discharge issued under this subchapter shall be held conclusive that the lien upon the property covered by the certificate is extinguished" does not bar relief to the Government

[1] In addition to contending he had made no misrepresentations in his application, Baker contended the income tax claim was barred by the statute of limitations and not filed within the time fixed by Section 57 (n), Bankruptcy Act. The referee found against all of Baker's contentions (R. 91a). The District Court did not pass on any of these questions.

in the courts where the discharge of the lien was secured through fraud; and (2) that the bankruptcy court had the power to grant the relief sought by the Government.

ARGUMENT

Petitioner urges that under Section 3675, Internal Revenue Code (Appendix, *infra,* p. 14), the certificate of discharge of the lien is conclusive, and that the Government may not invoke the familiar rule enabling an injured party to avoid a transaction because of fraud. We submit that this contention is unsound and that Congress did not intend to render inapplicable the well-established equitable principles under which a transaction may be set aside for fraud. The bankruptcy court certainly has the power to scrutinize the equities of claims filed in the proceedings and to subordinate or disallow claims of creditors who by their frauds secured an inequitable position over other creditors. *Pepper* v. *Litton,* 308 U. S. 295; *Taylor* v. *Standard Gas Co.,* 306 U. S. 307; *American Ins. Co.* v. *Avon Park,* 311 U. S. 138, 146; *Sampsell* v. *Imperial Paper Corp.,* 313 U. S. 215. In *Pepper* v. *Litton, supra,* a dominant stockholder obtained a fraudulent judgment against a corporation for the purpose of defeating claims of creditors. He perfected his judgment lien more than four months prior to bankruptcy of the corporation and the state courts, upon application of the injured creditor, refused to set

aside the judgment. By reason of his judgment lien, the stockholder would have nominal priority over other creditors of the bankrupt corporation in the bankruptcy proceedings. This Court held that the bankruptcy court, under its broad equitable powers, and because of the fraud, properly subordinated the stockholder's judgment lien to claims of other creditors. As this Court stated in *Sampsell* v. *Imperial Paper Corp., supra* (p. 219):

> The power of the bankruptcy court to subordinate claims or to adjudicate equities arising out of the relationship between the several creditors is complete.

Here, the bankruptcy referee in granting relief applied the same equitable principles as those used in the cases cited above. Equitable relief was awarded the Government by setting aside and vacating the certificates of discharge which had been secured through fraud, thereby giving the claims of the Government lien status and priority over petitioner as to the fund involved. Since no other creditors claimed any interest in the fund, only petitioner was affected by the relief granted. The result reached was the same as if the bankruptcy court had subordinated petitioner's claim to the tax claims of the United States by refusing to give lien status to petitioner's claim, in which event petitioner's claim would have been inferior to the tax claims of the United States even if they were not supported by liens, because of the provi-

sions of Section 64a (4), Bankruptcy Act, as amended (Appendix, *infra,* p. 11).

The bankruptcy court was the only tribunal in which the Government could secure adequate relief. The property had been sold by the trustee under order of the bankruptcy court and the trustee had possession of the proceeds of the sale. It was necessary for the bankruptcy court to determine the order of priority of claims filed in the proceedings, and to do so the validity of lien rights necessarily had to be passed on by the court. Section 2a (7), Bankruptcy Act, as amended (Appendix, *infra,* pp. 9–10); *Straton* v. *New,* 283 U. S. 318, 321; *Ray* v. *Norseworthy,* 23 Wall. 128.

Petitioner relies on *Arkansas Comm'n* v. *Thompson,* 313 U. S. 132. There, it was held that a bankruptcy court had no power to review an order of a state commission which had fixed the value of corporate property for state tax purposes, after hearing evidence as provided by the Act and where no appeal had been taken to the courts, although one was provided for by law. The power of the bankruptcy court to determine the amount and legality of taxes does not carry with it the power to revise property values fixed by the quasi judicial body pursuant to state law. The Act did not intend to give the taxpayer the privilege of two trials, in the state court and the federal court on an indentical issue of fact. There was no question of fraud involved and it was not

contended there was any irregularity in the proceedings before the Commission.

That case is therefore plainly distinguishable. Here, there was no attempt to retry a case in the bankruptcy court, after it had been heard and determined by another tribunal. The Government merely invoked the equitable powers of the bankruptcy court to grant relief on the ground that it had given up valuable lien rights, because of petitioner's fraud. The cases cited in petitioner's brief (p. 12) all involve different questions from the question here presented. None of these cases were concerned with the power of a bankruptcy court or court of equity to grant relief on the ground of fraud or other inequitable conduct, nor did any of them construe the provisions of Section 3675, Internal Revenue Code.

CONCLUSION

The decision of the lower court is correct and not in conflict with other decisions. The petition should be denied.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
SEWALL KEY,
HELEN R. CARLOSS,
HOMER R. MILLER,
Special Assistants to the Attorney General.

DECEMBER 1943.

APPENDIX

Bankruptcy Act of July 1, 1898, c. 541, 30 Stat. 544, as amended by the Act of June 22, 1938, c. 575, 52 Stat. 840, Sec. 1:

> SEC. 2. *Creation of Courts of Bankruptcy and Their Jurisdiction.*—a. The courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this Act, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to—
>
> * * * * *
>
> (2) Allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them against bankrupt estates;
>
> * * * * *
>
> (6) Bring in and substitute additional persons or parties in proceedings under this Act when necessary for the complete determination of a matter in controversy;
>
> (7) Cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided, and determine and liquidate all inchoate or vested interests of the bankrupt's spouse in the property of any estate, whenever under the applicable laws of the State, creditors

are empowered to compel such spouse to accept a money satisfaction for such interest;

* * * * *

(15) Make such orders, issue such process, and enter such judgments, in addition to those specifically provided for, as may be necessary for the enforcement of the provisions of this Act: *Provided, however,* That an injunction to restrain a court may be issued by the judge only;

* * * * *

b. Nothing in this section contained shall be construed to deprive a court of bankruptcy of any power it would possess were certain specific powers not herein enumerated. (11 U. S. C., 1940 ed., Sec. 11.)

* * * * *

SEC. 38. *Jurisdiction of Referees.*—Referees are hereby invested, subject always to a review by the judge, with jurisdiction to (1) consider all petitions referred to them and make the adjudications or dismiss the petitions; (2) exercise the powers vested in courts of bankruptcy for the administering of oaths to and the examination of persons as witnesses and for requiring the production of documents in proceedings before them, except the power of commitment; (3) exercise the powers of the judge for the taking possession and releasing of the property of the bankrupt in the event of the issuance by the clerk of a certificate showing the absence of a judge from the judicial district, or the division of the district, or showing his sickness or inability to act; (4) grant, deny, or revoke discharges; (5) confirm or refuse to confirm arrangements or wage-earner plans, or set aside the confirmation of arrangements or wage-earner plans and reinstate the proceedings or cases; (6) perform such of the duties as are by

this Act conferred on courts of bankruptcy, including those incidental to ancillary jurisdiction, and as shall be prescribed by rules or orders of the courts of bankruptcy of their respective districts, except as herein otherwise provided; and (7) during the examination of the bankrupt, or during other proceedings, authorize the employment of stenographers for reporting and transcribing proceedings at such reasonable expense to the estate as the court may fix. (11 U. S. C., 1940 ed., Sec. 66.)

* * * * *

SEC. 64. *Debts Which Have Priority.*— a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be * * * (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: *Provided,* That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: *And provided further,* That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States is entitled to priority and rent owing to a landlord who is entitled to priority by applicable State law; * * *. (11 U. S. C., 1940 ed., Sec. 104.)

* * * * *

SEC. 67. *Liens and Fraudulent Transfers.* * * *

b. The provisions of section 60 of this Act to the contrary notwithstanding, statutory liens in favor of employees, contrac-

tors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition in bankruptcy or of the original petition under chapter X, XI, XII, or XIII of this Act, by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court. * * * (11 U. S. C. 1940 ed., Sec. 107.)

* * * * *

SEC. 70. *Title to Property.*—a. The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition in bankruptcy or of the original petition proposing an arrangement or plan under this Act, except * * *. (11 U. S. C., 1940 ed., Sec. 110.)

Internal Revenue Code:

SUBCHAPTER B—LIEN FOR TAXES

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition

to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person. (26 U. S. C. 1940 ed., Sec. 3670.)

SEC. 3671. PERIOD OF LIEN.

Unless another date is speicfically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time. (26 U. S. C., 1940 ed., Sec. 3671.)

SEC. 3672. VALIDITY AGAINST MORTGATEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS (as amended by Sec. 401, Revenue Act of 1939, c. 247, 53 Stat. 862, and Sec. 505, Revenue Act of 1942, c. 619, 56 Stat. 798).

(a) *Invalidity of Lien without Notice.*—Such lien shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector— * * *. (26 U. S. C., 1940 ed., Sec. 3672.)

* * * * *

SEC. 3674. PARTIAL DISCHARGE OF PROPERTY.

* * * * *

(b) *Part Payment.*—Subject to such regulations as the Commissioner, with the approval of the Secretary, may prescribe, the collector charged with an assessment in respect of any tax may issue a certificate of discharge of any part of the property subject to the lien if there is paid over to the collector in part satisfaction of the liability in respect to such tax an amount determined by the Commissioner, which

shall not be less than the value, as determined by him, of the interest of the United States in the part to be so discharged. In determining such value the Commissioner shall give consideration to the fair market value of the part to be so discharged and to such liens thereon as have priority to the lien of the United States. (26 U. S. C., 1940 ed., Sec. 3674.)

SEC. 3675. EFFECT OF CERTIFICATES OF RELEASE OR PARTIAL DISCHARGE.

A certificate of release or of partial discharge issued under this subchapter shall be held conclusive that the lien upon the property covered by the certificate is extinguished. (26 U. S. C., 1940 ed., Sec. 3675.)

U. S. GOVERNMENT PRINTING OFFICE: 1943